

Michigan MI-1040

Additions and Subtractions

Issued under P.A. 281 of 1967. Filing is mandatory.

Schedule 1

Attach to form MI-1040. Please print or type clearly in blue or black ink.

Attachment Sequence No. 01

Primary Filer's First Name and Middle Initial	Last Name

▶ Primary Filer's Social Security Number

Additions to Income

- | | | |
|----|---|----|
| 1. | Gross interest and dividends from obligations issued by states other than Michigan or their political subdivisions | 1. |
| 2. | Deduction for taxes, on or measured by, income including self-employment tax deducted on your federal return (see p. 14)..... | 2. |
| 3. | Gains from Michigan MI-1040D and MI-4797..... | 3. |
| 4. | Losses attributable to other states (see p. 14)..... | 4. |
| 5. | Net loss from federal column of your Michigan MI-1040D or MI-4797..... | 5. |
| 6. | Other (see p. 14). Describe: | 6. |
| 7. | Total additions. Add lines 1 through 6. Enter <i>here</i> and on MI-1040, line 10 | 7. |

Subtractions from Income

- | | | |
|-----|---|-----|
| 8. | Income from U.S. government bonds and other U.S. obligations included in MI-1040, line 9..... | 8. |
| 9. | Military pay from U.S. Armed Forces included in MI-1040, line 9 (attach W-2).
(Include retirement pay on line 12 of this schedule)..... | 9. |
| 10. | Gains from federal column of Michigan MI-1040D and MI-4797..... | 10. |
| 11. | Income attributable to another state. Explain type and source: | 11. |
| 12. | Retirement or pension benefits included in MI-1040, line 9. (Include military retirement here.)
See exceptions, page 15. Name
of payer: | 12. |
| 13. | Dividend/interest/capital gains deduction for senior citizens (see p. 15) | 13. |
| 14. | Social Security benefits from U.S. 1040, line 20b or U.S. 1040A, line 13b..... | 14. |
| 15. | Income earned while a resident of a renaissance zone. Name of zone: | 15. |
| 16. | Michigan state and local income tax refunds received in 1998 that are included in MI-1040, line 9. | 16. |
| 17. | Miscellaneous subtractions (see p. 15). Describe: | 17. |
| 18. | Total subtractions. Add lines 8 through 17. Enter here <i>and</i> on MI-1040, line 12..... | 18. |

You must file an original form, a copy of this form, or a Treasury-approved substitute form.

Michigan MI-1040

Additions and Subtractions

Schedule 1

This is a new schedule for tax year 1998. In previous tax years the additions and subtractions were included as part of the *Michigan Income Tax Return* (MI-1040).

If you have additions to or subtractions from your adjusted gross income as reported on your U.S. 1040, 1040A or 1040EZ you must complete *MI-1040 Schedule 1* and attach it behind your MI-1040 form.

Please **separate** your MI-1040 and MI-1040 Schedule 1 at the perforation. Assemble your returns and attachments and staple in the upper left corner. A sequence number is printed in the upper right corner of the following forms to help you assemble them in the correct order behind your MI-1040 form.

- MI-1040 Schedule 1
- Direct deposit of refund (form 3174)
- Nonresident and part-year resident (Schedule NR)
- Farmland credit (MI-1040CR-5)
- Property tax credit (MI-1040CR or MI-1040CR-2)
- College tuition credit (Schedule CT)
- Federal schedules (see Table 1 on page 6 of the MI-1040 instruction booklet)
- Schedule of Apportionment (MI-1040H)

If you have questions call 1-800-487-7000. **Deaf, hearing or speech impaired persons** should call 517-373-9419 (TTY) for assistance.

Information and forms are also available on our web site at:
www.treas.state.mi.us

MI-1040 SCHEDULE 1

Part-year and nonresidents, complete Schedule NR (see page 19) before proceeding.

Additions to Income

Line 1: Enter gross interest, dividends, and income from obligations or securities of states and their political subdivisions other than Michigan. Add this income even if it comes to you through a partnership, S corporation, estate or trust. You may reduce this income by related expenses not allowed as a deduction by Section 265(a)(1) of the IRC.

Line 2: Enter the deduction taken for **self-employment tax** on your federal return and for other taxes on or measured by income, such as your share of city income tax paid by partnerships or S corporations, or your share of the taxes paid by an estate or trust.

Line 3: Use Michigan form **MI-1040D** if you have capital gains or losses attributable to: 1) an election to use Section 271 treatment for property acquired before October 1, 1967; 2) the sale or exchange of U.S. obligations which cannot be taxed by Michigan; or 3) the sale or exchange of property subject to allocation provisions.

If you reported gains on U.S. 4797 and acquired the property before October 1, 1967, adjust the gain on Michigan form **MI-4797**.

Instructions are with each form. Enter gains from the Michigan column of your MI-1040D, line 17, or MI-4797, line 18b.

Line 4: Enter losses from a business or losses from property located in another state which you own as a sole proprietor, a partner in a partnership or as a shareholder in an S corporation. If your business is taxed by both Michigan and another state, the loss must be apportioned. Attach a *Schedule of Apportionment* (form MI-1040H).

Line 5: Enter the net loss from the federal column of your Michigan MI-1040D, line 18 or MI-4797, line 18b.

Line 6: Enter the total of the following (attach a schedule if necessary):

- amount of net operating loss deduction (NOL carryforward) used to reduce AGI (see page 8)

- net loss included in AGI from Michigan gas and oil royalty interest or working interest
- refund received from a Michigan Education Trust (MET) contract. If you deducted the cost of a MET contract in previous years and received a refund from MET during 1998 because the MET contract was terminated and the beneficiary is not attending an institution of higher education, then enter the smaller of:

- a. the refund you received, **OR**
- b. the amount of the original MET contract price (including the application and processing fees) which you deducted in previous years.

If you financed your MET contract with a MET-secured loan, deducted the cost of that contract and then defaulted on the loan, enter the amount paid in 1998 by MET to repay the outstanding principal portion of your defaulted loan.

Subtractions From Income

Note: Part-year and nonresidents subtract only the applicable amounts included in income attributed to Michigan (column B of Schedule NR) on all lines except line 11.

Line 8: Enter income from U.S. government obligations (Series EE bonds, Treasury notes, etc.), including income from U.S. government obligations received through a partnership, S corporation or trust. This subtraction must be reduced by any interest expense on indebtedness incurred in carrying the obligation and by any related expenses used to arrive at AGI. Investment companies that invest in U.S. obligations are permitted to pass the tax-free exemption of such holdings to their shareholders. These shareholders are treated as owners of a proportionate share of the fund's assets.

If income from U.S. government obligations exceeds \$5,000, attach a copy of your U.S. *Schedule B* listing the amounts received and the issuing agency.

Capital gains from the sale of U.S. government obligations must be adjusted on Michigan form MI-1040D.

Line 9: Enter compensation received for active duty in the U.S. Armed Forces included in AGI. Include military retirement on line 12.

Note: A Michigan resident who receives compensation from the U.S. Public Health Service may not subtract the income as military pay.

Line 10: Enter the gains from the federal column of your Michigan form **MI-1040D, line 17 and MI-4797, line 18b**. Do not enter amounts from your federal forms. See instructions for MI-1040 Schedule 1, line 3.

Line 11: Income Attributable to Another State. Nonresidents and part-year residents, complete Schedule NR. See instructions on page 20. Attach federal schedules.

Business income from an activity that is taxable by Michigan and by another state must be apportioned. Complete and attach form MI-1040H.

Capital gains from the sale of real property located outside of Michigan must be adjusted on Michigan form MI-1040D.

Michigan residents cannot subtract salaries and wages or other compensation earned outside Michigan. However, you may be entitled to a tax credit for tax imposed by governmental units outside Michigan (see page 32).

Residents may subtract:

- business income derived solely in other states and included in AGI, and
- net rents and royalties from real property located or used in another state.

Line 12: Qualifying retirement and pension benefits that you included in your AGI may be subtracted from income. The amount you may subtract depends on the source of the benefit. Qualifying benefits include:

- pension plans that define eligibility for retirement and set contribution and benefit amounts in advance
- qualified retirement plans for the self-employed
- distributions from a 401(k) plan attributable to employer contributions or attributable to employee contributions to the extent they result in matching contributions by the employer
- IRA distributions received after age 59 1/2 or described by Section 72(t)(2)(iv) of the IRC
- benefits paid to a senior citizen (age 65 or older) from a retirement annuity policy which are paid for life (as opposed to a specified number of years)

- benefits from any of the previous received as a surviving spouse.

You may subtract **all** pension benefits included in AGI which are received from the following public sources:

- the State of Michigan
- Michigan local governmental units (e.g., Michigan counties, cities and school districts)
- tier 1 and 2 railroad retirements
- federal civil service
- military retirement from the U.S. Armed Forces.

If all retirement and pension benefits were received from public sources listed above, enter the total of all benefits on line 12. Benefits from any other source may be limited. See instructions below to compute the maximum subtraction.

If all retirement and pension benefits were received from private sources, enter the smaller of:

- the total of all private pensions included in AGI, or
- \$33,630 if you are a single filer, \$67,260 if you are married, filing jointly.

If you received a combination of public and private retirement and pension benefits, follow these steps to compute your deduction:

Step 1: Add all public retirement benefits included in AGI to compute the total amount of all public benefits received.

Step 2: If you are a single filer, deduct the amount in step 1 from \$33,630. If you are married filing jointly, deduct the amount in step 1 from \$67,260.

Step 3: Add all private pensions included in AGI to compute the total amount of all private benefits received.

Step 4: Determine which is smaller, the amount computed in step 2 or the amount computed in step 3.

Step 5: Add the amount computed in step 1 and the amount determined in step 4 together and enter the total on line 12. See Example A on page 16.

You may not subtract:

- Amounts received from a deferred compensation plan that lets the employee set the amount to be put aside and does not set retirement age or requirements for years of service. These plans include, but are not limited to plans under Section 457 and distributed under Section 401(k) of the Internal Revenue Code.

- Amounts received before the recipient could retire under the plan provisions, including amounts paid on separation, withdrawal or discontinuance of the plan.

- Amounts received as early retirement incentives, unless the incentives were paid from a pension trust.

Line 13: Senior citizens (age 65 or older) may subtract interest, dividends and capital gains included in AGI. This subtraction is limited to a maximum of \$7,500 on a single return or \$15,000 on a joint return, and must be reduced by the pension subtraction. See Example B on page 16.

Line 14: Enter only the taxable portion of Social Security benefits included on your U.S. 1040, line 20b, or your U.S. 1040A, line 13b. Do not include your total Social Security benefits.

Line 15: Renaissance zone deduction. To be eligible you must meet all the following requirements:

- Be a permanent resident of a renaissance zone for at least 183 days.
- Must not be delinquent for any state or local taxes abated by the Renaissance Zone Act.
- Must file an MI-1040 each year.
- Have gross income of not more than \$1 million.

If you were a full-year resident of a renaissance zone you may subtract all earned income. Unearned income such as capital gains may have to be prorated. If you lived in the zone at least 183 days during 1998, you may subtract the portion of income earned while a resident of the zone. Complete and attach a Schedule NR to your MI-1040. (See "Special Note" at the end of the Schedule NR instructions.) For additional information regarding qualifications for the renaissance zone deduction call

the Michigan Tele-Help System (1-800-827-4000) and listen to topic #293.

Line 16: You may subtract Michigan state and city income tax refunds and homestead property tax credit refunds that were included in AGI.

Note to farmers: You may subtract (to the extent included in AGI) the amount that your state or city tax refund and homestead property tax credit exceeds

the business portion of your homestead property tax credit.

Line 17: Allowable miscellaneous subtractions include:

- Contributions to national or Michigan political parties or candidates. The maximum deduction is \$50 on a single return and \$100 on a joint return.
- Benefits from a discriminatory self-insured medical expense reimbursement plan, to the extent these reimbursements are included in AGI.
- Proceeds and prizes won in State of Michigan regulated bingo, raffle or charity games to the extent included in AGI.
- Amount of salary and wage expense that cannot be deducted on your federal return because you are claiming a work opportunity credit, clinical testing (orphan drug) credit or research credit. Attach a copy of U.S. *Work Opportunity Credit* (form 5884), *Credit for Increasing Research Activities* (form 6765), or *Orphan Drug Credit* (form 8820) to substantiate this subtraction.
- Losses from the disposal of property reported in the Michigan column of Michigan form MI-1040D, line 18 or MI-4797, line 18b.
- Amount used to determine the credit for elderly or totally and permanently disabled from U.S. *Schedule R*, line 19, or U.S. *1040A Schedule 3*, line 19.
- Michigan net operating loss deduction. Attach MI-1045. See page 8.
- Net income included in AGI from Michigan gas and oil royalty interest or working interest.
- If you purchased a Michigan Education Trust (MET) contract during 1998, you may deduct the total contract price (including application and processing fees).
- If you purchased a MET payroll deduction or monthly purchase contract, you may deduct the amount paid on that contract during 1998 (not including fees for late payments or insufficient funds). You should receive an annual statement from MET specifying this amount.
- If you purchased a MET contract between 1988 and 1990 with a MET-secured loan and have not previously deducted the total contract price paid,

you may deduct the principle amount paid on the secured loan during 1998.

• Amount of taxable benefits the **purchaser** received and included in AGI during 1998 because the MET contract was terminated to attend a private school or out-of-state school, or the beneficiary (student) did not attend school. The beneficiary cannot claim this subtraction.

You may not subtract:

- Itemized deductions from U.S. *Schedule A*.
- Sick pay, disability benefits and wage continuation benefits paid to you by your employer or by an insurance company under contract with your employer.
- Unemployment benefits included in AGI, except railroad unemployment benefits.

- Distributions from a deferred compensation plan received while a resident of Michigan.
- Lottery winnings. (Exception: installment payments from prizes won on or before December 30, 1988 may be subtracted.)

EXAMPLE A: Computing pension deduction.

John and Karen Jones file jointly and received the following income during the 1998 tax year:

Michigan Public School Retirement System	\$12,000
Military Retirement Pay	\$ 8,000
General Motors Retirement Program	\$20,000
IRA Distribution	\$ 4,000

John and Karen are allowed to deduct the entire amount of pension income they receive from public/military retirement systems in determining Michigan taxable income. However, the maximum allowable private pension deduction must be reduced by the amount of public/military pension income claimed as a deduction.

Determining the private pension deduction:

Step 1: Add all public and military retirement benefits together. $\$12,000 + \$8,000 = \$20,000$

Step 2: Deduct the amount calculated in step 1 from \$67,260
(use \$33,630 if a single filer). $\$67,260 - \$20,000 = \$47,260$

Step 3: Combine the total amount of private pension income including IRAs. $\$20,000 + \$4,000 = \$24,000$

Step 4: Determine which is smaller: the amount computed in step 2 or step 3.
The \$24,000 from step 3 is smaller and is the allowable private pension deduction.

Step 5: Determine the total pension deduction by adding the amounts computed in step 1 and step 4.

Total public and military pension income	\$20,000
Total allowable private pension deduction	<u>24,000</u>
Total 1998 pension deduction. Enter on MI-1040 Schedule 1, line 12	\$44,000

EXAMPLE B: Senior Citizen Interest, Dividend, Capital Gains Deduction

Joe and Susan are both 67 and file jointly. They received the following income during the tax year 1998:

Capital Gains	\$10,000
Pension	\$ 2,000
Social Security	\$ 4,800
Dividends	\$ 500
Interest	\$ 2,000

They may deduct the \$2,000 pension on their MI-1040 and the senior citizen interest, dividend and capital gains income as shown in steps 1 through 3 below.

Determining the interest, dividend and capital gains deduction:

Step 1: Add all capital gains, dividends and interest income:

Capital Gains	\$10,000
Dividends	500
Interest	<u>2,000</u>
Total	\$12,500

Step 2: Subtract pension from the maximum capital gains, dividends and interest deduction of \$15,000 for joint filers (\$7,500 for single filers).

Maximum Deduction Amount	\$ 15,000
Less Pension Subtraction	<u>(2,000)</u>
Total	\$ 13,000

Step 3: Total interest, dividend and capital gains deduction is the smaller of the calculation from step 1 or step 2; \$12,500 is the allowable deduction. Enter this amount on MI-1040 Schedule 1, line 13.